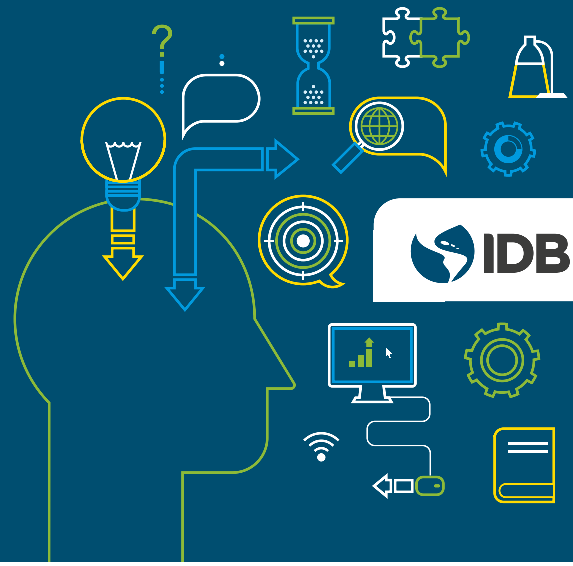
RESEARCH INSIGHTS



Is Business Dynamism Declining?

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- **Recent research shows a global decline in business dynamism, characterized by lower firm entry rates and slower job reallocation, particularly in advanced economies.**
- **The global decline in business dynamism is widespread across sectors, including the sectors that have been relatively more dynamic such as those intensive in information and communication technology.**
- **Demographic trends, such as the slowdown in working-age population growth, have the potential to explain the slowdown in business dynamism, as entry rates are closely linked to population growth rates. However, variation in population growth rates appears to account for only part of the decline in business dynamism.**

CONTEXT

Business dynamism has experienced stark and widespread decline, which could have major implications for the economic trajectory of many regions. In the United States, researchers have documented a long-term decrease in firm entry rates, job reallocation, and entrepreneurship, sparking debates about the causes behind these trends. This phenomenon has since been observed in other advanced economies, and more recently in less developed regions like Latin America and the Caribbean. The broad scope and consistent nature of these patterns across diverse economies have spurred growing interest in understanding the underlying factors and their broader economic impact.

PROJECT

The study explores how to better measure declining business dynamism—using indicators such as firm entry rates, job reallocation, and growth dispersion—to assess how dynamic markets foster productivity, innovation, and growth. The project also investigates potential drivers of this decline, including demographic shifts, rising market power, and technological advancements. By analyzing these trends, the research aims to form a comprehensive picture of what we know about the decline in business dynamism and understand its implications to delineate the role of policy in reversing the slowdown.

RESULTS

There is a significant decline in business dynamism across both advanced and developing economies over the past few decades. This decline is evident in lower firm entry rates, reduced job reallocation, and increasing market concentration. Recent evidence also points to similar trends in regions like Latin America and the Caribbean (LAC), where these indicators have historically been low. For instance, data from the OECD DynEmp Project (presented in Figure 1) show that, in the period of 2000 to 2015, Brazil and Costa Rica have experienced declines in job reallocation rates that are accompanied by reductions in entry rates, which signals reduced business dynamism.

Several factors drive this decline. Demographic changes, such as slower labor force growth, lead to fewer new firms and an aging firm structure, concentrating economic activity in larger, older firms. In this context, comparing entry rates between countries can be difficult, as entry rates in developing countries tend to be higher due to growing working-age populations, not necessarily because of more business dynamism (Figure 1).

Key Concept

ENTRY AND EXIT RATES

The percentage of new firms entering a market in a given year and the percentage of existing firms that cease operations during the same period.

Technological advances also play a role, with larger firms that invest in innovation growing faster and securing larger market shares, which further reduces dynamism. Globalization has contributed, as more productive firms expand into new markets, crowding out smaller firms.

Another key factor is market concentration and rising market power. Large firms benefit from regulatory advantages and strategic practices like patent thickets, which restrict competition and limit knowledge diffusion. Weakened antitrust enforcement and regulatory barriers, such as occupational licensing and non-compete clauses, exacerbate these issues by impeding competition and innovation.

POLICY IMPLICATIONS

Policymakers need to be aware of these trends to effectively address the challenges posed by the decline in business dynamism. A multifaceted approach focused on fostering competition, removing barriers to knowledge diffusion, and adjusting regulations to encourage entrepreneurship and economic growth is essential.

Robust antitrust enforcement is critical to preventing monopolistic practices. Policymakers should enhance monitoring and regulation of market power, particularly among large firms, to prevent them from stifling competition and innovation. This includes investigating potential anticompetitive behaviors and implementing policies that promote market entry for smaller firms.

Moreover, many existing regulations, such as occupational licensing and non-compete clauses, can impede new firm entry and limit innovation. Even tax laws can be inefficient and deter growth. Policymakers should conduct a thorough review of these regulations to identify and eliminate those that unnecessarily restrict competition and impair productivity. Simplifying the regulatory landscape will lower barriers for new businesses and encourage entrepreneurial activity.

Key Concept

MARKET POWER

Market power refers to the ability of a firm to influence prices and output levels in a marke, often assessed through metrics like market share or price markup.

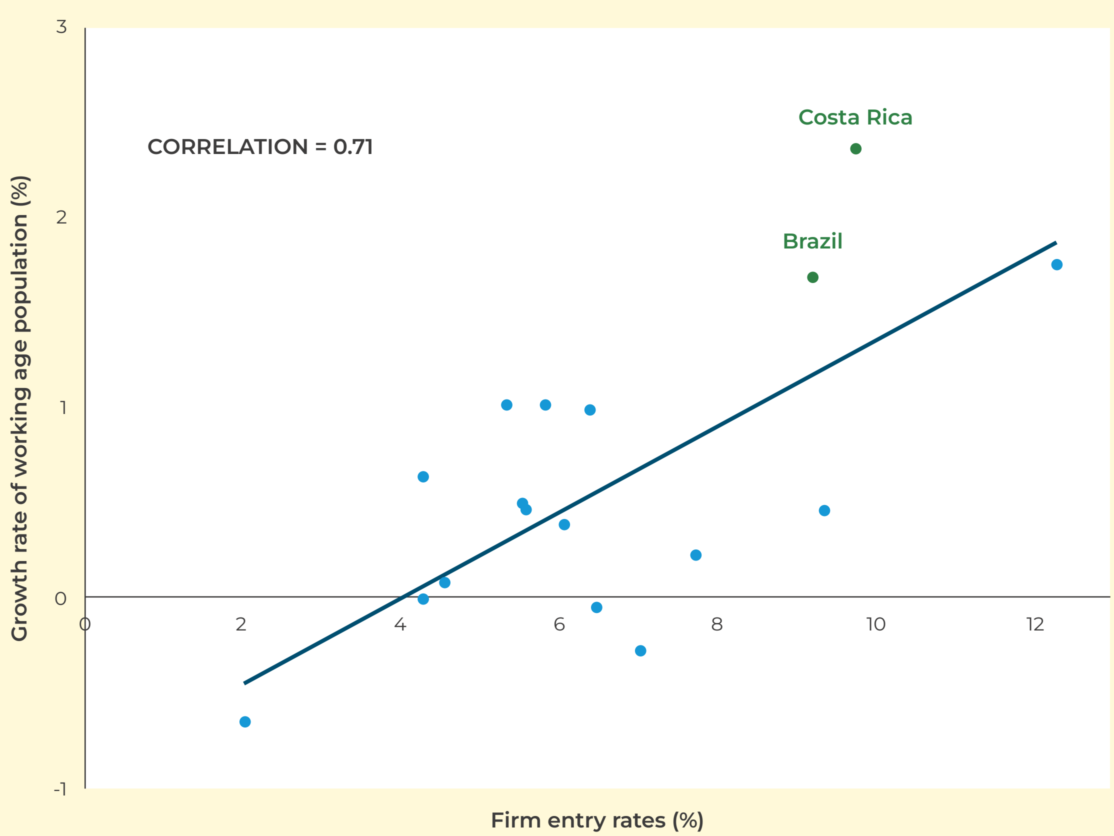
Finally, facilitating knowledge sharing among firms can drive innovation and, consequently, improve overall business dynamism. For instance, policymakers could support initiatives that promote open innovation, such as partnerships between large corporations and startups, and create platforms that enable smaller firms to access valuable data and resources. This will help level the playing field and foster a more competitive environment. In this regard, supporting entrepreneurship by targeted support for startups and small businesses could be very relevant. **Policymakers should consider initiatives that provide access to funding, mentorship programs, and incubators to foster entrepreneurial spirit.**

Key Concept

JOB REALLOCATION

The movement of jobs between firms and sectors, usually measured by the total number of jobs created through new hires plus the number of jobs lost through layoffs.

FIGURE 1. Firm Entry and Demographics



Source: OECD and OECD DynEmp Project.

Department of Research and Chief Economist

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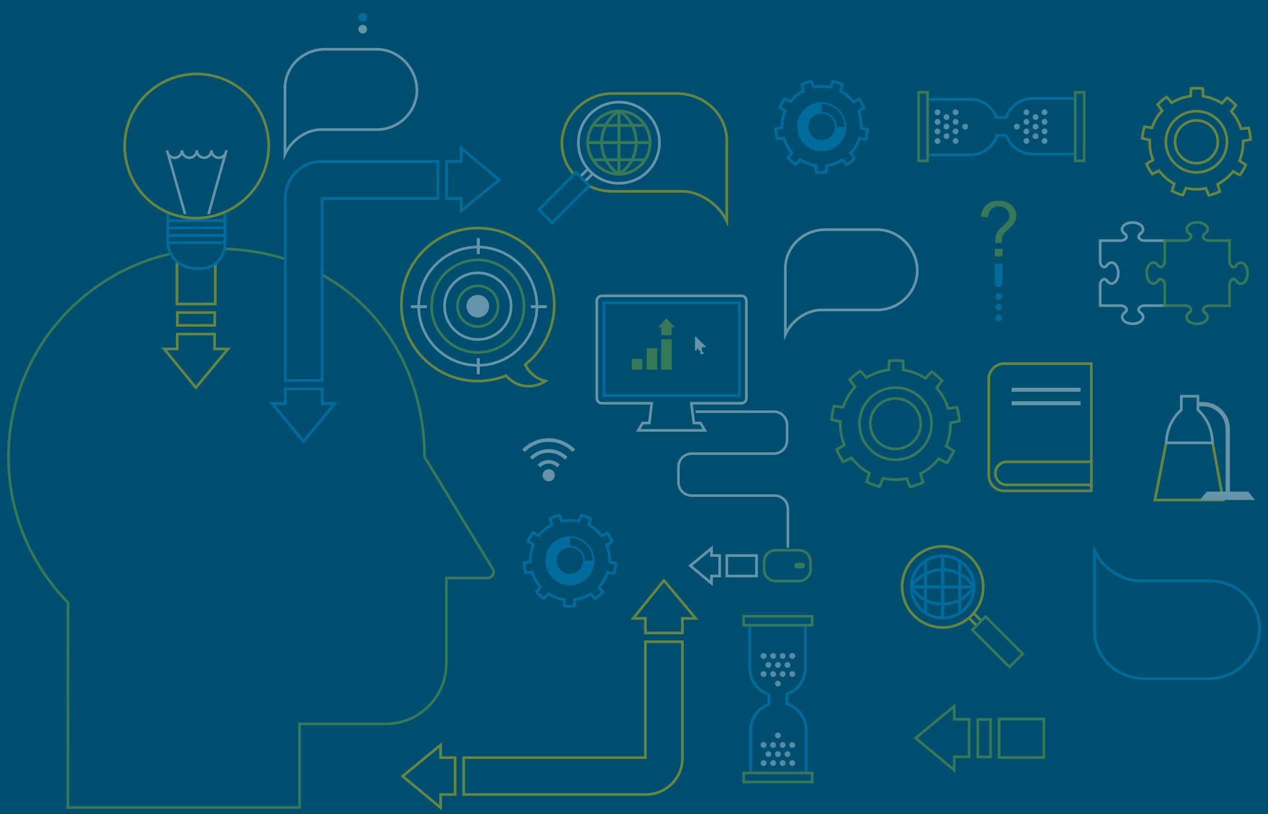

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